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AT DEADLINE

Callan loses Fulton County

Two Fulton County, Georgia, employee pension boards have reversed their earlier decision to hire Callan Associates Inc. as consultant because of concerns about political influence on the firm, as well as Callan's fees.

The Fulton County Employees' Pension Board and Fulton County General Employees' Pension Board will begin contract negotiations with Wyatt Asset Services.

Travelers seeks ruling

The Travelers Corp. has filed suit in federal court in Hartford, Conn., asking the court to determine the proper method of liquidating and distributing assets to investors in Travelers Insurance Co.'s troubled Separate Account R open-end commingled real estate fund.

The Travelers suit comes on the heels of a suit filed by the Dallas Police and Fire Pension Fund accusing Travelers of fraud, misrepresentation and breach of fiduciary duty.

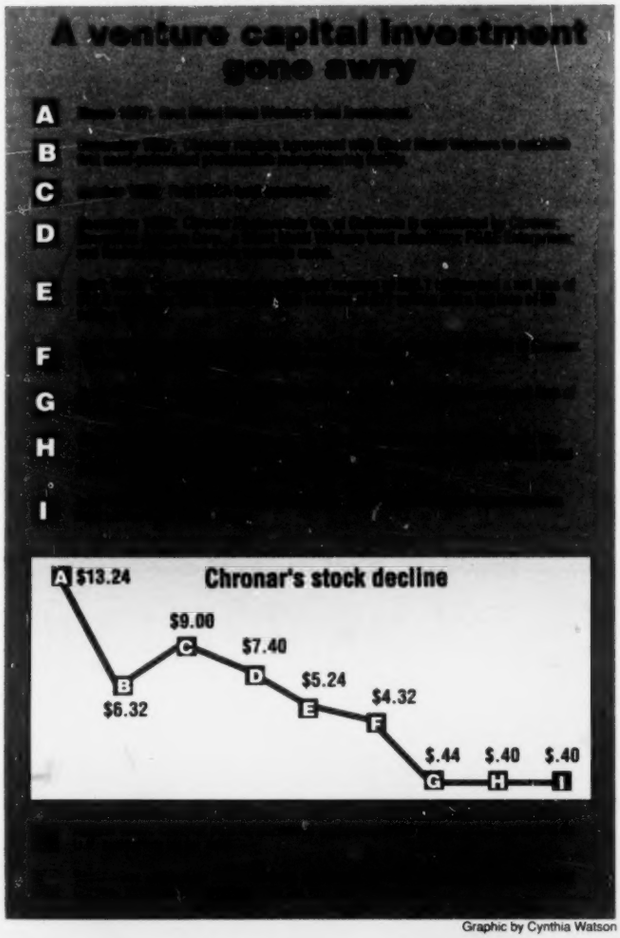
Managers pick up accounts

The $850 million San Bernardino County Employees' Retirement System has selected Mellon/McMahan Real Estate Advisors Inc., San Francisco, to manage its $93.4 million real estate portfolio, replacing The Yarmouth Group Inc. . . . The $300 million Employees' Retirement System of the City of Norfolk, Va., has awarded $50 million each to fixed-income managers Western Asset Management and Lowe, Brockenbrough, Tierney & Tattersall. It renewed an account with Gardner & Preston Moss and terminated Wentworth, Hauser & Violich. . . . The $1.65 billion Idaho Public Employees Retirement System has hired Globe Finlay Inc. to actively manage a European portfolio.

INSIDE

Is that all there is?

Contrary to popular belief in the investment community, Rule 144A was not designed to enlarge private placements' slice of the capital markets and so should not be considered a flop.
Commentary, Page 16.



Graphic by Cynthia Watson

$85 million stake up against the wall

By Hillary Durgin

Two multibillion-dollar union pension funds' $85 million venture capital stake in a solar energy company is on the line as the company faces possible bankruptcy.

During the past three years, the Sheet Metal Workers' National Pension Fund and the National Electrical Contractors Association Pension Benefit Trust Fund have invested their pension assets into Chronar Corp., Lawrenceville, N.J. The two funds own a total of 78.2% of the company's stock — an extraordinarily high stake for pension funds.

The investments strongly suggest a desire by the funds to create jobs for union members, a social investing practice that could run afoul of the private pension

See **Unions** *on page 48*

Funds shift target for proxy season

New focus put on directors

By Marcia Parker

Two public pension funds are among the institutional investors launching campaigns in advance of the 1991 proxy season that will shake up boards of directors.

"The difference this season will be the focus on boards of directors. It's a clear shift in direction, which stems from the institutional investors' view that the most important thing is to elect a board to represent them," said Peg O'Hara, director of the corporate governance service at the Investor Responsibility Research Center, Washington.

Activist investors are focusing attention on how boards perform and how independent they are, and to open a direct line of communication with the boards.

The California Public Employees' Retirement System, one of the most activist in the nation, has sent letters and questionnaires to the 4,600 directors of the Fortune 500 companies.

Richard Koppes, general counsel, said the fund is asking directors what criteria should be used to evaluate the performance of directors and companies, whether directors should own stock in the companies they help run and whether the chief executive officer should be chairman of the board.

The pension fund also solicited views on state laws protecting companies from takeovers, and asked directors whether they'd like to be considered for other boards.

The letter stresses the fund won't use the data to determine how to vote on a nominee. "Our goal here is to develop and disseminate information about directors and director candidates and to encourage the election of the best qualified people we can find," the letter says.

The fund also invited the directors to communicate directly with the pension fund. The data will be used to build a data base with Institutional Shareholder Services Inc., profiling all the directors of companies in the Standard & Poor's 500 Stock Index. It would be the first time such extensive data would be compiled.

Institutional investors also will be sponsoring several different shareholder resolutions relating to board activities for the first time in the 1991 season.

"We see the board of directors as the main focus," Mr. Koppes said. "We will more carefully review our vote for directors next year and publicize that vote. We want to put some more light . . . on the independence of directors and the need for boards to be composed of a majority of outsiders."

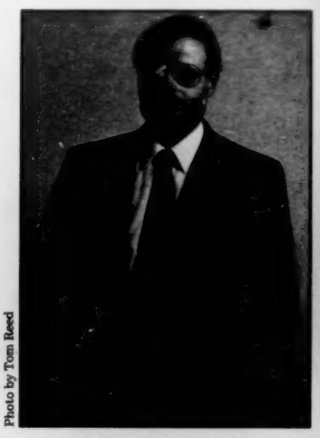


Photo by Tom Reed

Richard Koppes said his fund is seeking standards to evaluate director performance.

The California fund is sponsoring its first shareholder resolution to require a majority of the company's board to be independent, as defined by the Council of Institutional Investors: Someone who has not been employed by the corporation or an affiliate in an exec-

See **Proxy season** *on page 50*

FMC ups interest in distressed securities

By Marlene Givant Star

CHICAGO — Marshaling their investing experience with distressed securities, executives for the $1 billion FMC Corp. retirement plans increased the commitment to the talked-about but largely uncharted asset class.

For six years, FMC has been investing its defined benefit plan — and for two years, its defined contribution plan — in distressed securities, an area most large pension funds are only beginning to examine. While the investments make up an insignificant portion of the total retirement assets, which are split roughly evenly between defined benefit and defined contribution plans, they are viewed as an important component of the philosophy that has placed FMC in the top 1% of large funds in the SEI Capital Resources Co. performance universe for the 10-year period ended Dec. 31.

FMC's defined benefit plan returned a compound annual 18% for the 10 years ended Dec. 31.

FMC recently made its first investment specifically in the distressed area, committing 2% of its defined benefit assets to the Zell Chilmark limited partnership fund.

To date its existing distressed securities investments have been part of diversified portfolios, including a mutual fund for the defined contribution plan called Mutual Qualified Income Fund managed by Heine Securities Corp. in Short Hills, N.J., and a separate account for the defined benefit plan managed by Peter Cundill & Associates, Vancouver, British Columbia. In both cases, distressed investments do not exceed 20% of the portfolio, with the rest in stocks and bonds.

The motivation for distressed securities investment "obviously

See **FMC** *on page 50*

NEWS DIGEST

Michael Dubrow has joined NCM Capital Management Group as vice president and operational head of the firm's new guaranteed investment management division, which will emphasize the active development and use of GIC synthetics. Page 41.

Southern Co.'s David Prince and six other executives join Delaware Investment Advisers' operations. Page 4.

SEI Corp. has reorganized by target markets rather than by products. Page 6.

SPECIAL REPORT: PUBLIC FUNDS

Officials overseeing the investments of public pension systems face a myriad of issues — from social investing to maintain the plans funded status and ways to increase diversification. Page 21.

FINANCING

Middle Market Group has undergone a management buy-out, but the firm will continue to serve midsize companies. Page 37.

More than 300 corporate debt issuers were downgraded during the first three quarters of 1990. Page 39.

INTERNATIONAL

Units of Unisys and Dow Chemical are among the Swiss firms adapting higher equity exposures. Page 3.

PanAgora Asset Management landed new accounts for the pension funds of G. Heileman Brewing and TRW and Nuclear Mutual's general account. Page 32.

Global asset allocators have shown a superior ability to move money and markets. Page 35.

REAL ESTATE

Pension funds' property commitments should hold firm, the new Emerging Trends report finds. Page 34.

Callan Associates has surprised some investors with its finding that separate realty accounts provide almost double the return of commingled funds. Page 2.

DEPARTMENTS

Classified	48	Pension Surplus Index	12
Commentary	16	P&I Age indexes	10
Frontlines	9	Portfolio management	36
Letters	16	Software	44
Money movers	42	Valuation index	13
Opinion	14	Washington	40

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Top 1,000 Funds survey in progress

Pensions & Investments' **annual survey of the Top 1,000 pension funds in the nation is under way. Questionnaires have been mailed for the directory, which will be published in the Jan. 21 issue. The deadline is Nov. 11. If you have not received a questionnaire, or have a question regarding the form, please contact Christine Philip, directory coordinator, at (312) 649-5217.**

Reversion coup de grace

Bill's tax provisions spell end for plan terminations

By Joel Chernoff

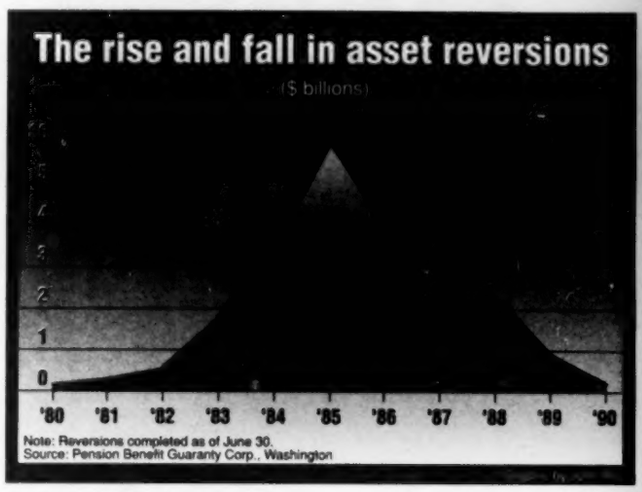
WASHINGTON — Chalk up another practice of the 1980s that has bit the dust: terminations of overfunded pension plans.

Nine years after the new German owners of the A&P supermarket chain recouped a large part of their investment by terminating the company's overfunded pension plan, the practice effectively has been snuffed out by Congress.

While Congress has debated the issue, employers have terminated nearly 2,200 overfunded plans, recapturing more than $21 billion in surplus assets.

In the budget-reconciliation bill expected to be passed by Congress last week, the excise tax on surplus assets could soar as high as 50% from the current level of 15%. Add the corporate income tax rate of 34%, and terminations will become prohibitively costly for all but those companies in dire need of cash.

"This is probably the end game for the termination reversion issue," said David M. Walker, national director-compensation and benefits, Arthur Andersen & Co., Washington, and a former Reagan administration pension official.

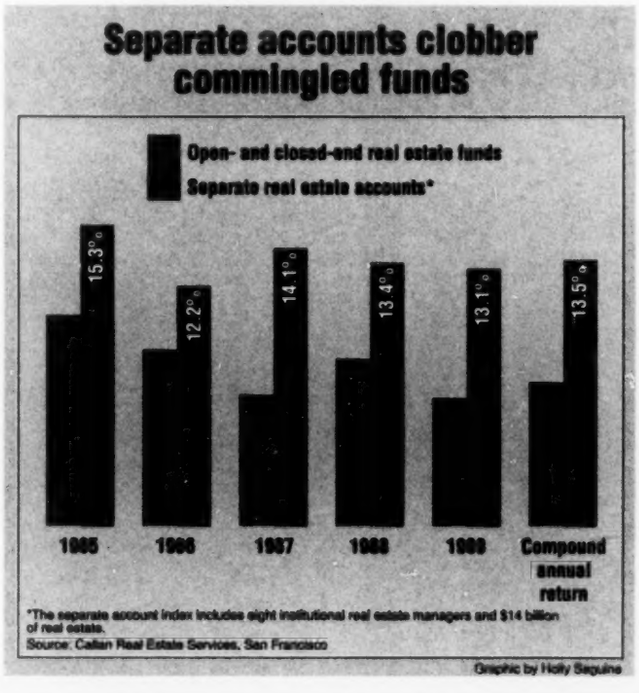


Basically, the bill would raise the basic excise tax to 20%. But under the House version, which was expected to prevail, employers would have to use 30% of the surplus as a cushion in a replacement plan or face an additional 30% excise tax. Employers in liquidation proceedings would be exempt from the additional tax.

Most employers would be expected to set up a new plan. Because only the reversion and not the cushion would be subject to

See **Budget** *on page 47*

Gap found in realty returns



By Steve Hemmerick

Pension funds using real estate separate accounts get almost double the investment returns of commingled real estate funds, Callan Associates says.

Real estate separate accounts scored a 13.5% compound annual return between 1985 and 1989, vs. 7.3% for commingled funds, according to Callan, a San Francisco-based consulting firm. Callan's statistics came from its client data base.

The separate account performance contradicts some pension executives' contention that real estate in general has not performed well during the past several years. But the numbers also support — and likely will escalate — the move by pension funds to separate accounts and away from commingled funds.

This year, for the first time, tax-exempt investors — mostly larger pension funds — tipped the real estate asset balance to 50.4% in favor of separate accounts.

Meanwhile, the high return for real estate separate accounts surprised some investors: Unlike

See **Returns** *on page 46*

Health-cost reporting speeded

By Fred Williams

A little-known SEC staff accounting bulletin could force companies to disclose their accrued liabilities for retiree medical costs as early as next year.

According to a 1987 Securities and Exchange Commission letter, companies should discuss the effect "of impending accounting changes . . . to inform the reader about expected impacts on financial information to be reported in the future."

A spokeswoman at the SEC said the staff letter "is not binding" but "most companies regard it as authoritative."

She said companies that already have assessed their liability under the proposed accounting standard on post-retirement medical benefits by the Financial Accounting Standards Board, or have forecast the future impact on financial statements, "should disclose the information."

While it might not be binding, accountants are acting as if it were. "If the information is available, you would have an obligation to disclose the effect," said Tom Elliot, audit partner with the accounting firm of Arthur Andersen & Co., Atlanta.

In the 1987 letter, the SEC concluded companies should comply with disclosure requirements for accounting standards that have been issued but do not become effective until some future date because the existence of the stan-

See **Surprise** *on page 47*

INTERNATIONAL

Batterymarch sees green in Soviet venture

■ When it came to perestroika, people probably didn't think of Boston's Batterymarch Financial Management. How times have changed.

Earlier this month, Batterymarch unveiled its Soviet Companies Fund, a cooperative venture between Batterymarch and the USSR's State Commission on Military Industrial Production. The new fund will be seeking investments of between $400 million and $1 billion from no more than 20 corporations around the world covering 10 industries.

Through the Soviet Companies Fund, these companies would hold stakes in a subsidiary of a larger Soviet enterprise which will be converted from a producer of military goods to a provider of consumer and other non-defense products.

Participation in the fund should "help global companies find out about opportunities in the Soviet Union," said David Gill, trustee at Batterymarch. Once companies "get a glimmer" of the opportunities in the USSR, they might go on their own developing these opportunities, he said.

The fund itself is intended to last three years — after which participants would have the right to liquidate. This could happen in two ways: Either each investor would get a pro-rata share of the fund's portfolio; or, if participants all agreed, they could have an auction bid among themselves for the fund's assets.

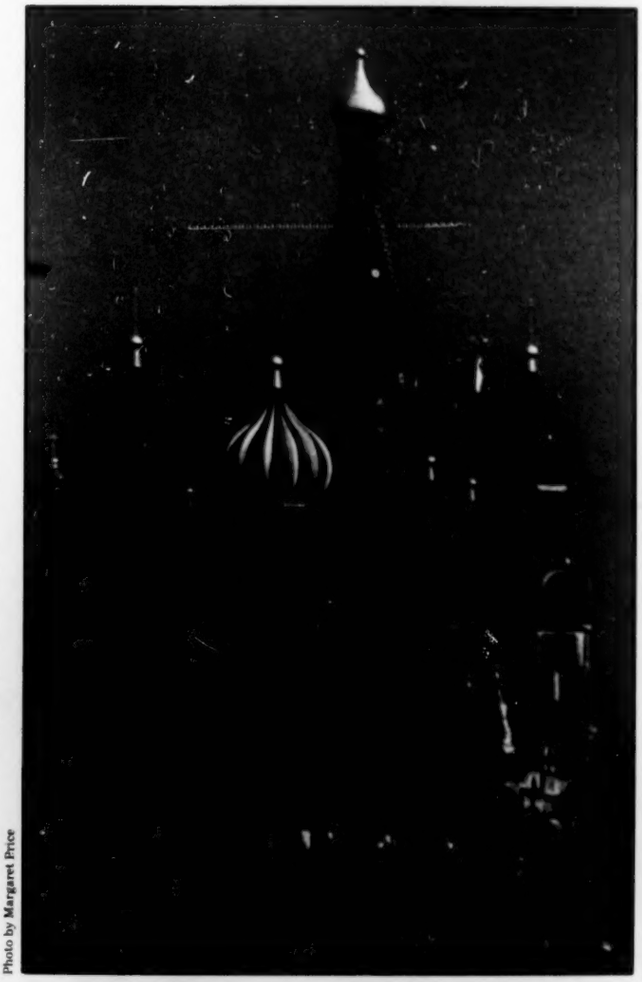


Photo by Margaret Price

Up to 20 corporations are being sought to invest in a venture that will help Soviet companies convert to consumer goods production.

WASHINGTON

Firms win contracts for auditing

■ Two accounting firms and an actuarial firm firms pulled down federal contracts to audit governmental retirement programs.

KPMG Peat Marwick's Washington office and Metcalf, Zima & Co., Atlanta, were picked by the Department of Labor to review adherence with federal fiduciary standards for the $10 billion federal Thrift Savings Plan.

KPMG Peat Marwick also will review the records of Wells Fargo Nikko Investment Advisors, San Francisco, and the U.S. Treasury that relate to the plan's stock and bond index funds. Metcalf, Zima will conduct selected audits of federal payroll and personnel sites around the country.

While the thrift plan is overseen by the Federal Retirement Thrift Investment Board, the Department of Labor has responsibility to regulate the fund.

Separately, Facciani & Co., Cleveland, won a government contract to perform an independent audit of the actuarial valuation of the Social Security Administration's Old-Age, Survivors and Disability Insurance program.

REAL ESTATE

Good deals are where you find 'em

■ Some institutional real estate investors, straying from their traditional approach of buying specific property types in specific markets, now say finding a good deal for any property type anywhere is their goal.

That's one of the conclusions of Chicago-based Real Estate Research Corp.'s third-quarter investment survey. *Pensions & Investments* will publish highlights of RERC's survey each quarter.

Among those specifying property preferences, industrial lost its top rank for the first time in more than two years, edged out by retail. Although some investors continue to favor regional malls, others now prefer community or neighborhood centers with at least one strong anchor tenant and good cash flow. In addition, power centers — shopping centers from 250,000 to 600,000 square feet with at least 60% of the space devoted to three or four anchor stores — were mentioned for the first time as the retail investment of choice.

Apartments, meanwhile, continue to garner increased investor interest, growing from the top preference of 6% of respondents during the first quarter of 1990 to 20% during the third quarter.

Investors' pre-tax yield expectations range from a low of 10% for regional malls to 13% for suburban office buildings. The median yield is beginning to rise; its current level of 11.5% is 50 basis points higher than year-end 1989.

Investors remain reluctant to project growth in income streams. In fact, most projections assume no growth in the first two to five years of a project, with only modest increases after that.

"No matter how intelligently a diversified portfolio of investments has been assembled, sooner or later the weakness of the real estate market will take its toll," the RERC survey concludes.

Top property preferences

	3rd qtr. 1990	2nd qtr. 1990	1st qtr. 1990	3rd qtr. 1989	3rd qtr. 1988
Industrial (%)	32	44	55	71	53
Retail (%)	36	38	28	21	32
Office (%)	12	-	11	8	16
Apartments (%)	20	19	6	-	-

Source: Real Estate Research Corp., Chicago

PRIVATE PLACEMENTS

He isn't playing the Rule 144A game

■ While investment bankers are touting the virtues of the new private placement market under the Securities and Exchange Commission's Rule 144A, one longtime investor is disgusted with the whole affair.

"So far, all Rule 144A has done is diminish many of the most attractive aspects of privately placed securities, namely their negotiated protective covenants and call protection features," said Frederic Feuerherm, vice president-bonds of MIMLIC Asset Management, St. Paul, Minn., which has invested in private placements for more than 25 years.

"MIMLIC will not be a participant in the so-called 'new 144A market' where these features appear to be watered down," he added.

In the name of promoting greater liquidity, 144A is making privately placed transactions too standardized, doing away with the market practice of lender participation in negotiations and documentation, he said.

The private market always has been free of strict reporting and disclosure requirements. But that can be problematic when an issuer is from a foreign country that doesn't require extensive reporting of financial data or with companies whose information essentially must be taken at face value.

MIMLIC manages $5.6 billion; of that, $1.6 billion was in private placements as of Dec. 31.

Rule 144A was designed to make the secondary private placement market broader and more liquid by defining qualified buyers and waiving the previous two-year restriction on trading of the securities. It also exempted U.S. and foreign corporations from registration requirements on the resale of stock and bond offerings to qualified buyers.

Frederic Feuerherm believes Rule 144A is hurting protection features for investors.

MERGERS & ACQUISITIONS

Japanese pull back on volume of megadeals

■ Japanese companies scaled back megadeals in the United States during the first nine months of this year, slashing M&A volume to $4.1 billion, a fraction of the $11.1 billion at the end of September 1989.

According to DealScope, the mergers and acquisitions data base of Ulmer Brothers Research Institute, New York, the number of acquisitions and investments by Japanese companies in the United States increased 5% to 139, but volume dropped sharply because of the absence of very large deals.

Two large pending deals — the bid for MCA Inc. by Matsushita Electric Industrial and the acquisition of Southland Corp. by Ito-Yokado Co. and Seven-Eleven Japan Co. — would add almost $8 billion to the 1990 total.

To date, approximately half of the transactions have been acquisitions and half have been investments. The value of the acquisitions, at $2.3 billion, heavily outweighs the $1.5 billion in investments. The remain $300 million consists of joint venture buyouts and division purchases.

The mix of industries targeted by the Japanese was quite narrow. Three sectors — financial services, chemicals and computers — accounted for two-thirds of the deal volume.

PEOPLE

Sole trusteeship splits candidates

■ One issue New York State Comptroller Edward Regan and his Democratic challenger Carol Bellamy are locking horns over is Mr. Regan's position as sole trustee of the $47 billion New York State & Local Retirement Systems.

If Ms. Bellamy, who is on leave from her job as a public finance banker at Morgan Stanley Inc., wins Nov. 6, there likely will be major changes in the way the big New York pension fund is run.

Mr. Regan has been in office for 12 years, and faces what even he acknowledges as his toughest opponent. Running the pension fund is only one of the comptroller's jobs; he is the state chief's fiscal officer.

Still, New York is one of only a few states where the pension fund is overseen by a sole trustee who is an elected official.

Ms. Bellamy has proposed creation of a seven-member board of trustees to manage the fund's investments.

Mr. Regan, who is well known in the public and corporate pension fund community, has himself called on the state Legislature to change the sole trustee system. The retirement system does have an advisory board.

Ms. Bellamy has said little about her stand on activism by public pension funds on corporate governance and social issues. Mr. Regan has been a behind-the-scenes player on governance initiatives, preferring to focus on the board of directors and one-on-one talks with portfolio companies. Under his stewardship, the pension fund has sponsored many shareholder resolutions on social issues such as Northern Ireland and South Africa.

Returns

Continued from page 2

commingled fund performance, separate account returns generally aren't published and are less widely known.

Callan officials say the separate account performance figures are significant because they are based on extensive property holdings valued at $14 billion.

They also said investors routinely might expect returns 300 to 400 basis points higher over time from direct separate accounts invested in core real estate than from commingled fund invested in core real estate. (Core real estate investments generally are top-grade, fully leased urban office and large retail properties, but sometimes include leased warehouses and apartments.)

Not all real estate professionals concur with Callan's findings.

Dennis Miller, manager of venture capital and real estate of the $2.5 billion Atlantic Richfield Co. pension fund, has found real estate separate account investment performance to be significantly higher than that of commingled funds. But he said a 620-basis point spread between the two — as Callan reported — sounds "a little high."

John Koza, a consultant for real estate and a senior vice president with The Frank Russell Co., Tacoma, Wash., questioned whether reported investment returns for separate accounts and commingled funds are analogous.

Separate account performance calculations aren't standardized, whereas commingled fund performance calculations are to some extent, he said.

In addition, some separate account properties are appraised only once every three years, whereas commingled fund properties generally are appraised at least once a year. And, Mr. Koza said, separate account numbers might include some items that wouldn't be tabulated as income in commingled fund returns.

"I would be concerned about drawing any major conclusions from (Callan's) numbers," he said.

Mr. Koza didn't say what he thinks separate account returns might be in a typical portfolio. He said returns would be influenced by the risk and reward guidelines established for a particular investor.

Todd Kurtin, a manager for Management Advisory Services with Kenneth Leventhal & Co., Los Angeles, said he wonders how the commingled and separate account returns could be so different when typically the advisers are the same for both types of accounts. He noted fees would account for some of the difference.

Jack Barthell, a partner at Leventhal, suggested some of the spread between separate accounts and commingled funds might be explained by the growing sophistication of advisers.

When commingled funds started, said Mr. Barthell, advisers had more of a "broker" orientation. They lacked some of the analytic, economic and market research and asset management skills they have today, he added.

Because many of the separate account investments were made subsequent to problems in the oil patch states, some separate accounts might have avoided investment in many properties that suffered subsequent sharp declines, Mr. Barthell said.

ARCO's Mr. Miller noted his pension fund, one of the first to establish a separate account for real estate, did invest in some oil belt properties, but the separate account still outperformed commingled funds.

Callan officials said their numbers for separate accounts were reported by investment advisers.

According to Callan, the spread between returns on separate accounts and commingled funds could result partly from clear directions and close monitoring by the pension investor.

Trustees for the Los Angeles County Retirement Association referred to the higher separate account returns recently when they called in executives from Prudential Real Estate Investors, Newark, N.J., and Sentinel Real Estate Corp., New York.

Company executives tried to dissuade the trustees from leaving Prudential's PRISA I fund and Sentinel's SRE fund.

The trustees listened attentively, but still followed the recommendation of Callan — their consultant — and voted to join the queue of pension funds waiting to get their money out.

They also voted to leave Equitable Real Estate Investment Management Inc.'s Prime Property Fund, a large open-end pooled investment vehicle like the two other funds.

Both Equitable's and Prudential's funds have some of the best investment returns among open-end commingled funds.

Sentinel's SRE fund has had less performance success lately, but it is 80% invested in one of the most popular property types, apartments.

In all, the Los Angeles trustees will take $59 million in core real estate holdings out of the open-end commingled funds. They also plan to exit some of their closed-end funds, when possible.

The trustees didn't make their decision to exit the open-end funds simply because of higher returns. They also expect to gain control over their assets and lower advisers' fees.

Still, substantially higher return numbers could be a powerful and convincing new incentive for pension funds to accelerate their move into separate accounts.

Decisions to leave commingled funds isn't necessarily all bad news for real estate advisers. Many of them later win back their old clients through separate accounts.

But the move to separate accounts could put additional downward pricing pressure on real estate advisory fees. With separate accounts, plan officials can better negotiate fee arrangements with real estate advisers.

Negotiation is often more difficult or impossible with commingled funds because assets are pooled and fees have to be charged equally.

More pension funds in separate accounts could create a kind of two-tier fee structure, with larger investors paying lower costs.

For the Los Angeles fund, the predicted fee savings is sizable — $4.5 million annually when all of its real estate assets are managed in separate accounts with a 10% allocation to real estate, Callan officials estimate.

According to Callan, commingled fund real estate fees are typically 1.25% of assets under management. Separate account fees, they said, are typically 0.8%, or 45 basis points lower.

By moving to a separate account, trustees also gain greater

See **Returns** *on page 49*

Pensions&Investments

P R E S E N T S

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- ▶ International Private Placements
- ▶ Non-U.S. Real Estate
- ▶ Selecting International Money Managers

Stocks

ntinued from page 3

The company's asset allocation
dy last year led to a strategy of
% equities (30% Swiss and 20%
reign), 40% in cash and Swiss
nds and 10% in foreign currency
nds, said Mr. White. He said be-
re the reorganization, the Unisys
hweis fund had 15% in equities.
"We're funding long-term liabi-
ies," Mr. White pointed out.
he Swiss company is very prof-
able and can take this added
sk, and we expect we can im-
ove benefits or lower contribu-
ns because of this strategy."
Dow Europe S.A., Horgen, a
it of Dow Chemical Co., reacted
the rule change by lifting its
uity investing target to 50%
m 30% of assets, said Wolfgang
chs, portfolio manager. Be-
use of unfavorable markets, the
proximately $140 million fund
has about 35% in equities and 15%
in cash. "But when the opportu-
nity allows, we'll get to the 50%
limit," said Mr. Fuchs.

"Pension liabilities generally
increase about 15% a year. There-
fore, we need higher returns to
cover at least part of this liability
increase every year," he said.

The fund is enjoying success
with its strategy. According to Mr.
Fuchs, the Dow fund usually posts
a better performance than the
best portfolios of the BVG index
of Pictet & Co.

Executives for the IBM Swit-
zerland pension fund, Zurich, re-
sponded to the law change last
year by increasing the fund's
"strategic allocation to interna-
tional equities," said Walter
Haab, vice president. While he
didn't say to what the new alloca-
tion was, he did say that over time
the fund planned to move "close
to the allowable limit."

"We have been rather high in
equities already, but proportion-
ately lower in international, as
compared with domestic equi-
ties," he said.

The approximately $125 million
fund of du Pont International
S.A., Geneva, has no targeted
asset allocation. But the company,
which has been using insurance
contracts, "has decided to use
more active management," said
Jack Stair, senior consultant-fi-
nance, E.I. du Pont de Nemours
& Co., Wilmington, Del. "We will
continue to use insurance for (an
undefined) portion of the fund but
will begin to use active manage-
ment, it's fair to say, for the ma-
jority of assets."

While the fund has selected
money managers, Mr. Stair wouldn't
cite how many firms, or which ones,
were chosen. Changes are expected
to take effect in January.

The review of pension investing
came because company executives
"had a sense that the maturity of
the plan would support higher-
risk investments," said Mr. Stair. ■

Unions

ntinued from page 48

e-seat executive committee.
During the next nine months,
e Sheet Metal Workers moved
protect its earlier investments.
e fund guaranteed up to 75% of
$10 million revolving line of
edit to Chronar issued by Na-
nal Bank of Washington. Har-
rt Solar, an Alabama solar
mpany, and its affiliate, Har-
rt International, guaranteed re-
yment of the remainder of the
edit line.
In exchange for the guarantees,
e fund and Harbert received
sh fees and warrants to pur-
ase company stock. Chronar of-
red as collateral a security in-
rest in its finished goods
ventory, accounts receivable
d other assets.
But the fund's involvement
ew. In December 1987, the com-
ny entered into a marketing,
anagement and consulting
reement with the pension fund
establish the company's first
miautomated 10-megawatt pho-
voltaic manufacturing facility
Fairfield, Calif.
Instead of manufacturing panels
cording to the labor-intensive
atch process," the much-vaunted
ureka" technology would produce
nels along a semi-automated pro-
ction line.
Through a wholly owned sub-
diary of the Sheet Metal Work-
s, Energetics Jungere Corp., the
nd agreed to pay $13 million for
e facility's equipment. Chronar
reed to operate the facility for
ronar Photovoltaic Co. of Cali-
rnia, a newly formed joint ven-
re between Chronar, with a 4%
ake; Energetics Jungere, 67%;
G&E Enterprises, a subsidiary
Pacific Gas & Electric, 27%;
d Bechtel Development Co., 2%,
nominee name.
The facility is supposed to be
mpleted by the third quarter of
91. A PG&E spokesman, how-
er, said PG&E dropped out of
e joint venture, while Mr. Wil-
ms said, "I'm confident they
e still involved."

Electrical workers enter

In October 1988, 18 months
ter the Sheet Metal Workers
ade its first major investment in
ronar, the electrical workers'
nd purchased $10 million of
ronar's common stock through
rivate placement.
That investment also gave the
d the right to invest in any of
ronar's future manufacturing
power-station projects in the
ited States, the company's
1988 annual report said.

The electrical workers also ob-
tained two seats on Chronar's
board and one on the executive
committee. Christina Samson,
who now serves as investment
manager, and Jack F. Moore,
trustee, were appointed to the
board, expanding the number of
board members to 13 from 11.

In the first five months of 1989,
the union funds buoyed their in-
vestments in Chronar with addi-
tional stock purchases and a se-
ries of loans worth more than $7
million. The Sheet Metal Workers
fund and Harbert also guaranteed
a $10 million revolving line of credit
issued by Midlantic National Bank,
Edison, N.J., which had replaced
National Bank of Washington as the
firm's lead bank.

The company's fortunes were tak-
ing a turn for the worse. Losses in-
creased to $12.8 million in 1988
from $8.9 million the year before.

Chronar hired turn-around ex-
pert Mr. Palmieri to assess the
company's prospects and strategy.

Mr. Palmieri said the company
would need a $30 million cash in-
fusion and an overhaul of its se-
nior management. Mr. Kiss re-
signed as chairman and chief
executive officer and became vice
chairman, while the board hired
Mr. Palmieri to run the company,
contingent on the company ob-
taining the new financing.

The funding chiefly was provided
by the two unions, each of which
bought $14.5 million of cumulative
convertible redeemable preferred
stock. Now, the Sheet Metal Work-
ers fund owned 34.24% of Chronar,
and the electrical workers fund
owned 39.25%, if the two funds were
to exercise their warrants and op-
tions.

Also, Renaissance Holdings PLC,
London, provided $1 million to
Chronar in exchange for convertible
debentures.

As part of the deal, The Palmieri
Co. received an option to purchase
shares of a newly issued series of
preferred stock.

But things didn't work out well.
While Mr. Palmieri had a three-year
contract with Chronar, he resigned
in June. Later, Chronar's chief
operating officer and its chief finan-
cial officer stepped down. So did
three board members: both repre-
sentatives from the electrical work-
ers' fund and Harbert's representa-
tive.

While the Palmieri group brought
a clear focus to the Eureka manu-
facturing project, Chronar could
neither afford nor justify the type of
expertise Mr. Palmieri typically
provided, Mr. Williams said.

"The company needed to be re-
duced in size to a very small en-
tity clearly focused on getting Eu-
reka financing," Mr. Williams
said. "I don't think it fit in with
what the Palmieri Co. wanted to
be doing." Mr. Palmieri declined
to comment for this story.

Bankruptcy discussed

By August of this year, how-
ever, Chronar's situation had be-
come dire. In its second-quarter
statement, the company said it
would have to suspend all of its
operations or seek protection
from creditors under federal
bankruptcy laws unless it re-
ceived a cash infusion within two
weeks. At the time, the company
said it needed an additional $15
million to continue operations
through the end of 1990 and $10
million in 1991.

A month later, a small piece of
that cash arrived — $2.15 million
from Energetics Jungere, as its
last installment in a $4 million
purchase of Chronar's Eureka
technology. Chronar has leased
back the technology from the
fund's subsidiary; Chronar has
the right to repurchase the tech-
nology for $4 million plus a small
stake in Energetics Jungere it had
acquired as part of the transac-
tion. But it needs $15 million to
exercise that right.

Most of the company's hopes
are riding on the the Eureka tech-
nology. Projected to be completed
by the third quarter of 1991, the
10-megawatt facility, small by
utility standards, is supposed to
provide electricity at a competi-
tive price, Mr. Williams said.

But Chronar's cash is only ex-
pected to tide over the company
until mid-November, he said.

The company now is operating
on a restricted spending plan.

The Sheet Metal Workers fund's
continuing rounds of investments in
a company taking continuing turns
for the worse raise questions.

"The basic issue is, 'Has this deal
turned sour' " said Michael S. Gor-
don a Washington pension attorney.
"Even if it was prudent at the out-
set, is it prudent now?"

In addition, the Sheet Metal
Workers' multiple transactions
might pose problems under the 1974
Employee Retirement Income Secu-
rity Act.

If Chronar is deemed a contri-
buting employer to the fund — some
of its operations were organized by
the Sheet Metal Workers — it could
be deemed to violate ERISA's pro-
hibitions on dealing with a party in
interest.

"You can't deal with a party in
interest," said Ivan Strasfeld, direc-
tor-office of exemption determina-
tions at the Department of Labor.
"You can't buy, sell, or hold in the
absence of exemption." ■

Respect

Continued from page 3

later, a Nobel Prize.

His theory, known today as the keystone of Modern Portfolio Theory, and Mr. Sharpe's elaborations have spawned a whole generation of financial analysts whose work affects trillions of dollars of market investments.

Mr. Markowitz theorized that optimal portfolios could be built that would enhance returns by reducing risk. The riskiness of individual securities was not important in themselves, he said. Instead, using mean variance analysis, he focused on the risk of the entire portfolio and showed how diversification would reduce it and enhance returns.

Mr. Sharpe is credited with the development of the Capital Asset Pricing Model, the theory that risk could be split into two parts. Stocks in themselves posed what he called unsystematic risk. That risk could be lessened through diversification, per Mr. Markowitz's theory.

Where Mr. Sharpe took off from Mr. Markowitz was in the concept of beta, or systematic risk. Beta is the measure of variation of stock prices due to the movement of the market as a whole. No matter how diversified the portfolio, there would always be market risk.

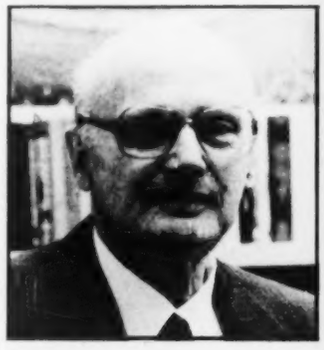
The theories have played a major role in the development of asset allocation models in use around the world.

"To me, Harry was the inventor, the man tinkering in the garage, and Bill is one of a number of really creative people who have taken that invention and run with it," said Keith Ambachtsheer, a Toronto-based consultant who has worked on further elaborations of Modern Portfolio Theory. "The reason I'm particularly pleased that Bill has won the award is that he's probably worked on it longer and harder than anyone else."

While Mr. Markowitz has concentrated on teaching and developing computer languages for applications to business problems, Mr. Sharpe has taught, written textbooks, developed software and now runs a consulting firm, William F. Sharpe Associates, based on implementing his theories.

The men's work came at a time when employee benefit plans were in their infancy; as the pension plans have grown to trillions of dollars, the guidelines the men set proved to be the basis for further writings, inventions and discussion around which investment decisions have been made.

Their theories — particularly Mr. Sharpe's focus on beta — have been challenged as the science of financial economics has matured and the ability of computers to explore their work has exploded. When Mr. Markowitz was writing a book based on his dissertation, computer data were input on punch cards, and he had only time to perform calculations on the relationships of 10 stocks. Now, hundreds of thousands of relationships can be performed in a day.



Harry Markowitz

"Nowadays, the world is different, but that doesn't mean any individual shouldn't move to minimize risk," Mr. Markowitz said.

"The history of ideas is never that someone comes up with something and that's it," Mr. Sharpe said. "You have to look at the whole stream of ideas and ask if it is better because this idea was in it."

To Mr. Ambachtsheer, the lasting value of the theories is evident in their use. They had little impact in the 1970s, he said, partly because the computer was in its infancy and also because of resistance from established economists.

"It needed a new generation that was comfortable with the mathematical approach to investing," he said. "The inventions came at a time when everything was in its place. The world in which they lived was a world of fixed exchange rates. Now, with the floating exchange rates, it is more important how you allocate your assets. Eventually, everyone has to do it."

What also will last is the thrill of winning the Nobel Memorial Prize in Economic Science.

Mr. Sharpe was tracked down in Tucson, where he was awakened at 3 a.m. by a phone call from the committee in Sweden. "This is the most one could ever reasonably hope to aspire to," he said.

Mr. Markowitz was tracked down in Tokyo, where he is teaching a semester at the University of Tokyo, taking a respite from his finance professorship at Baruch College of the City University of New York.

"Every person's dream in this field is to win the Nobel Prize," he said. "But what shook me up the most was the genuinely warm congratulations we've received and the enthusiasm with which my six kids are taking this," he said.

"It's sort of like the Chicago Cubs had won the pennant." ■

Returns

Continued from page 46

liquidity and control over their real estate assets, according to Callan officials.

Control has become increasingly important as several pension funds have been locked into administrative snarls trying or threatening to get out of some commingled real estate pools.

Control is a reason the San Francisco City & County Employees Retirement System is adding real estate separate accounts.

Clare Murphy, chief executive officer, said San Francisco's investment return should benefit through reduced separate account fees, although she couldn't say by how much.

She's more concerned with the investment structure.

In a commingled fund, she said, "you are not only dealing with the difficulties of the real estate market, you are also dealing in a structure that puts you at the mercy of the other participants, the owners of the other shares." One problem with open-end funds is getting equal treatment, she noted, while in closed-end funds, the investor often must deal with high fees, little liquidity and set investment structures.

An early investor in commingled funds, San Francisco has put $200 million in separate accounts in the past two years. ■